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Taxation Of Americans Residing Abroad

Prepared by the
Tax Policy Subcommittee
Republican National Committee's
Advisory Council on
Economic Affairs

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Dear Friend:

The United States is faced with increasing competition from the economies of other countries. This situation is amply demonstrated by our huge balance of trade deficit. America must be prepared to fight for its rightful share of world markets by using every resource at her command. One weapon in this battle is the presence of American business personnel abroad to promote the interests of the United States in international commerce.

However, our country's tax laws concerning its overseas citizens actually discourage Americans from living abroad. Supported by the Carter Administration, these policies exacerbate the balance of trade problem and cause a loss of jobs for Americans here and in foreign countries.

The following statement "Taxation of Americans Residing Abroad" written by Charles Breecher, a former State Department official, David MacDonald, a former Assistant Secretary of the Treasury and businessman Mack Mattingly, all members of the Republican National Committee's Economic Affairs Advisory Council, Subcommittee on Tax Policy, clearly demonstrates the pernicious effects of the current law and suggests legislation be enacted to cure the problems as stated in this paper.

I hope you will find this useful reading on a most important topic.

Very truly yours,

Chairman
Republican National Committee

The cumulative balance of trade deficit during the three years of the Carter Administration has been over ninety-two billion dollars. This figure represents an alarming export of jobs because every dollar spent abroad means one dollar less spent in the domestic economy in hiring employees of American business. This situation, however, can be greatly alleviated by the presence of American workers in foreign countries. The ability of American companies to place their representatives on foreign soil has three major positive effects:

1. It increases the volume of United States' exports because Americans residing abroad tend to order United States goods and services for both personal and business use.
2. It facilitates future business for United States companies by establishing commercial relationships built up through personal contacts.
3. It trains Americans in international business techniques. All these factors when taken together, mean jobs for Americans both at home and abroad.

Yet, despite the beneficial effects of American citizens residing in foreign countries, the Carter Administration advances policies which actually discourage that presence. Chief among these is the excessively high taxation of non-resident citizens of the United States. This policy initiated in 1976 with the enactment of the Foreign Earned Income Act is out of step with the rest of the world. Of the major industrialized nations, only the United States taxes its citizens on income they earn abroad. Other nations recognize that their non-residents pay substantial taxes to their foreign hosts in return for the services that the host countries provide and that for the home country to additionally tax its citizens living abroad is a form of double taxation. Instead, the United States opts for a complicated system of granting a dollar for dollar tax credit against United States income taxes and a partial exclusion from gross income of the cost of living differential between the United States and the non-resident's host country. Although the system sounds fair in theory, it breaks down in practice due to the fact that many countries have tax systems differing

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greatly from our own. It is a common misconception that the foreign tax credit precludes any unfair tax burden and that an exemption from taxation on foreign-source income or any other relief for non-residents is unjustified. This position might have merit if the tax credit were allowed for all taxes paid to a foreign country. Unfortunately, the credit applies only to the income tax, creating an unfair tax burden.

Unlike the United States, most countries of the world rely on indirect taxes, such as the value added tax (VAT) and other forms of sales and excise taxes. Most of these indirect taxes when levied by the United States or the individual states and local governments are deductible for a resident taxpayer, but equivalent taxes levied by foreign governments are not deductible for a non-resident American. Consequently, it is not only possible but probable that despite the tax credit, a non-resident American will be subject to more aggregate tax than will a resident with identical income. This discourages Americans from wanting to live abroad. Yet, the Carter Administration adamantly maintains that there is no tax discrimination against these foreign-based citizens. In a report issued on August 27, 1979, the Office of Management and Budget stated, "The numerous provisions of the Internal Revenue Code and regulations pertaining to Americans living overseas do not treat those citizens unfairly compared to citizens living in the United States."

In order to make foreign assignments attractive, United States corporations are required to pay its American personnel higher wages to offset the higher United States tax burden, thereby increasing their costs in the international marketplace. As a result, so that they may be competitive with foreign corporations with lower personnel costs, United States corporations have had to turn to residents of their host countries or third party nationals to meet their employment needs. These non-Americans do not tend to buy "American" when ordering equipment and services for their "overseas" contracts.

A recent study conducted by the J. A. Jones Construction Company showed that in the Mid-East "a U.S. contractor would have to pay a middle-management American employee $62,500 for that person to take home $27,480. By a comparison, a West German contractor would have to pay its manager $36,700 and that would net him a $29,244 income."

The impact of this disparity can be readily seen. "U.S. corporations—especially construction contractors—have been hurt. . .as they are finding that they must increase their bids substantially in order to cover the higher costs that they are forced to pay their American employees. American contractors have found themselves in a non-competitive position since the 1976 act took effect. There has been a substantial dropoff in the number of Middle East contracts that are being awarded to American firms. During the period from June 1975 through April 1978, for example, U.S. firms received contracts in the Middle East totaling approximately $8.9 billion, or approximately 10 percent of the $86 billion which was awarded during this period. However, from May 1978 through June 1977, after the Foreign Earned Income Act of 1976 had taken effect, U.S. contracting firms received only $346 million in contracts in the Middle East, which was a mere 1.5 percent of the more than $21 billion which was available." 1

The loss of revenues further increases our balance of trade deficit which has already been exacerbated by our large oil import bill. Any revenues to the federal treasury which have been derived from the Foreign Earned Income Act have been diminished by the fact that there are fewer and fewer Americans overseas to pay such taxes.

The Congress of the United States should recognize the serious impediment to American jobs that our present tax policies cause. Congress should enact legislation such as H.R. 5211 which would tax Americans abroad on a co-equal basis with their foreign counterparts. Such legislation will boost domestic employment and help lessen our balance of trade deficit, at practically no cost and almost all benefit.

1 *Honorable Bill Frenzel,* Congressional Record, *February 6, 1980.*

Background

Ten Advisory Councils and Committees were formed by the Republican National Committee in 1977 to update and redefine Republican positions and initiatives on national issues and to foster participation in guiding the future course of the Party and Republican candidates.

The Five Advisory Councils are Human Concerns, Economic Affairs, General Government, Natural Resources, and National Security and International Affairs. The Advisory Committees cover Campaign Services, Outreach, Communications, Fiscal Affairs, and Legal Affairs. The councils and committees are further divided into 30 subcommittees which deal with specific issues and problems.

Through frequent statements, the Advisory Councils and Committees will communicate positions and initiatives to Republicans, elected officials and the American public.

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